Q3 2023 Tapestry Inc Earnings Call - Final

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Body

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Presentation

OPERATOR: Good day, and welcome to this Tapestry Conference Call. Today's call is being recorded.

(Operator Instructions) Please note this call may be recorded. At this time, for opening remarks and introductions, I would like to turn the conference call over to the Global Head of Investor Relations, Christina Colone.

CHRISTINA COLONE, GLOBAL HEAD OF IR, TAPESTRY, INC.: Good morning. Thank you for joining us. With me today to discuss our Third Quarter Results as well as our strategies and outlook are Joanne Crevoiserat, Tapestry's Chief Executive Officer; and Scott Roe, Tapestry's Chief Financial Officer and Chief Operating Officer.

Before we begin, we must point out that this conference call will involve certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act. This includes projections for our business in the current or future quarters or fiscal year. Forward-looking statements are not guarantees, and our actual results may differ materially from those expressed or implied in the forward-looking statements.

Please refer to our annual report on Form 10-K, the press release we issued this morning and our other filings with the Securities and Exchange Commission, for a complete list of risks and other important factors that could impact our future results and performance. Non-GAAP financial measures are included in our comments today and in our presentation slides. For a full reconciliation to corresponding GAAP financial information, please visit our website. *www.tavestry.com/investors* and then view the earnings release and the presentation posted today.

Now let me outline the speakers and topics for this conference call. Joanne will begin with highlights for Tapestry and our brand. Scott will continue with our financial results, capital allocation priorities and our outlook going forward. Following that, we will hold a question-and-answer session, where we will be joined by Todd Kahn, CEO and Brand President of Coach. After Q&A, Joanne will conclude with brief closing remarks.

I'd now like to turn it over to Joanne Crevoiserat, Tapestry CEO.

JOANNE C. CREVOISERAT, PRESIDENT, CEO & DIRECTOR, TAPESTRY, INC.: Good morning. Thank you, Christina, and welcome, everyone. As noted in our press release, we delivered strong revenue, margin and earnings growth in the third quarter, significantly outpacing expectations. This demonstrates the power of brand building, customer centricity and our agile operating model. Importantly, we continue to advance our long-term strategic agenda, creating lasting customer relationships around the world through product innovation and compelling omni-channel experiences. A testament to the ingenuity of our talented global teams who continue to drive our results.

Touching on the strategic and financial highlights of the quarter. First, we powered global growth achieving 9% constant currency revenue gains, meaningfully surpassing our outlook. These top line results were led by our international businesses, which grew nearly 20% excluding FX. This included a greater-than-anticipated inflection in Greater China, where sales increased 20%, supported by a strong rebound in traffic and returning to growth compared to the region's peak fiscal '21 levels. Importantly, given our history in the market and the brand building investments we've made, our brands are well positioned to capture the opportunity with the Chinese consumer, both in Greater China and around the world.

In the quarter, we also drove continued momentum in Japan and other Asia with sales growth of over 20% as well as a mid-single-digit increase in Europe. In North America, sales rose low single digits against an increasingly challenging consumer backdrop. Of note, these results benefited from growth in January as we anniversaried more acute COVID-related disruptions in the prior year. Taken together, we delivered strong sales growth globally, while driving higher growth and operating margins compared to prior year, underscoring our commitment to being disciplined stewards of our brands and business.

Second, we continue to build lasting customer relationships. During the quarter, we acquired over 1.2 million new customers in North America alone. Importantly, these new customers transacted at higher AUR than the balance of our customer base and approximately half of these customers were Millennial and Gen Z, consistent with our strategy to attract younger consumers to our brands. At the same time, we reactivated lapsed customers across the portfolio.

Third, we delivered seamless omni-channel experiences, harnessing the power of our direct-to-consumer business model and highlighting our ability to meet consumers where they are shopping. We drove 10% growth in direct-to-consumer sales on a constant currency basis. This was led by low-teens growth in brick-and-mortar sales as we welcome an increasing number of consumers to our stores. In addition, digital sales rose mid-single digits and remained over 3x ahead of pre-pandemic levels.

Fourth, we fueled fashion innovation and product excellence informed by data, analytics and consumer research. To this end, we drove handbag AUR growth globally and in North America, which supported our gross margin increases in the quarter. We also delivered outsized gains in our small leather goods and lifestyle offerings, key to enhancing brand relevance and fueling customer value over time. Taken together, we generated third quarter earnings well above our expectations, rising over 50% compared to the prior year which we accomplished despite a volatile demand backdrop and currency headwinds. Based on this performance, we are raising our outlook for the fiscal year, underscoring our ability to drive sustainable, profitable growth.

Now turning to the highlights across each of our brands, starting with Coach. We outperformed expectations in the third quarter as we continue to build strength on strength. We drove an 11% revenue increase at constant currency, while delivering over 300 basis points of operating margin expansion fueled by gross margin gains. Throughout the quarter, we advanced our strategic initiatives, bringing expressive luxury to life.

First, we built on the momentum of our leather goods offering, extending our iconic families to drive consumer engagement. Tabby was again a top performer, resonating with both new and existing customers with notable success in the core shoulder bag. During the quarter, we launched new styles, including the Tabby Box bag, which provided silhouette diversification as well as the fun and nostalgic Jelly tabby, which drove strong sell-through specifically with younger consumers. In the Road family, our top handle silhouette gained momentum, becoming the #1 style within the collection. At the same time, Willow drove significant volume while Bandit outperformed expectations at elevated price points. In addition, we're creating compelling and emotional small leather goods assortment. As a result, we drove outsized growth in the category aided by success across wallets and micro bags in keeping with current trends.

Overall, our product innovation supported by the use of data and consumer insights throughout the product creation process fueled a high single-digit global handbag AUR growth at constant currency, including gains in North America. Second, we focused our marketing investments on brand-building activities, connecting emotionally with customers through the unique purpose of the brand. Building on Coach's courage to be real mission, we debuted our latest marketing that connects product and purpose. Our In My Tabby campaign featuring Lil Nas X, alongside a cast of global brand ambassadors redefines what we carry, not just in terms of physical objects but the experiences, journeys and aspirations that shape who we are.

Importantly, our 360-degree activation efforts supported the acquisition of approximately 800,000 new customers in North America alone, with over half being Millennial or Gen Z. We also drove strong engagement with existing clientele and reactivated lapsed customers, reaffirming our ability to attract new customers while retaining our existing customer base. And in China, we drove strong growth and brand momentum, capitalizing on Coach's leadership positioning and track record of success since entering the market 2 decades ago. During the quarter, we were pleased with the performance of our collaboration with the Nostalgic White Rabbit Candy brand, which debuted a celebration of Lunar New Year. This collection successfully drove the acquisition of new customers with over half of its purchasers being new to the brand.

Third, we drove a strong top line increase in our lifestyle offering, an area of long-term opportunity for the brand. In ready-to-wear, we delivered outsized growth with success across genders as we leaned into the key branding

elements. This performance was led by our compelling outerwear selection anchored by the brand's iconic trench. In men's, double-digit constant currency gains were fueled by our leather goods offering, aided by the continued strength of our Gotham family as well as the successful launch of the relay tote offered in a range of colors and featuring Coach New York graphics.

Fourth, we created omni-channel experiences that resonate with consumers by communicating our brand purpose of self-expression. We tested new experiential and immersive retail concepts across the globe, creating opportunities for customers to engage their senses throughout their brand and product discovery journeys. In Chicago, we launched Coach Play, the first in a series of concept stores, encouraging customers to play in coach spaces. These highly interactive locations, which we have since opened in Japan and Singapore, are bespoke, balancing design elements of the brand's heritage with local elements to connect with each store's community.

Further, we leaned into the success of our Tabby family to create Tabby shops in select stores around the world. These compelling environments utilize existing store architecture and were inspired by traditional ice cream shops to celebrate the different flavors of this iconic handbag collection. We also showcased these pop-ups across our digital channels, allowing the brand to scale the experience to a broader audience. And just last month, we were excited to officially launch Coachtopia, a sub-brand created with the goal of reimagining and disrupting the fashion industry. By working with a community of partners, including Gen Zs, we kept circularity as our North Star, delivering a line of products crafted from reused leather bags and recycled materials.

While a small assortment today, we are extremely pleased with the response to the product and purpose and see further opportunity ahead. In closing, Coach continues to differentiate both in its brand positioning and its financial performance. This success is rooted in the brand's magic. Its unique DNA and iconic product offerings, blended with the logic of deep customer understanding. Importantly, through expressive luxury, we're writing Coach's next chapter by connecting our history and purpose with innovative product and experiences, enabling self-expression for modern consumers around the world. We are confident in our strategy and the opportunity to deliver continued healthy growth for years to come.

Now moving to Kate Spade. Our third quarter results outpaced expectations, supported by revenue gains on a constant currency basis and gross margin expansion. At the same time, we made further foundational investments that are supporting our long-term strategic growth agenda. Positioning the brand to be more emotional, more lifestyle and more global in order to drive customer connectivity and deliver profitable growth. Touching on the details of the quarter. First, we remain focused on delivering an innovative and distinctive core handbag offering. The Knott remained the top global handbag group, while the recently introduced Hudson, which features wear-to-work styles was a recruitment driver for younger consumers.

In addition, the iconic sandbag offered in recycled nylon drove strong growth. The success of this family highlights the opportunity to engage consumers by leaning into the brand heritage and innovation. We also amplified our novelty offering, bringing heightened emotion and newness to the brand. The sheepdog collection resonated with both new and existing customers. In fact, this was the #1 full-price novelty style in the quarter, priced at nearly $500. Overall, our product initiatives, coupled with our use of data to deepen our understanding of consumer preferences, supported low single-digit handbag AUR growth at constant currency, both globally and in North America.

Next, we advanced our strategy to become more lifestyle, delivering strong revenue growth in the assortment, led by momentum in ready-to-wear, footwear and jewelry. Importantly, we continue to see that customers who shop across categories are our highest value customers, demonstrating the importance of the brand's lifestyle offering as a long-term growth driver.

Now touching on marketing. We expressed the world of Kate Spade through unique storytelling. In celebration of the brand's 30th anniversary, we leaned into its DNA as a beloved lifestyle brand that sparks Joy. To do this, we increased our top of funnel marketing spend, targeting Millennial and Gen Z consumers to support the reimagination of our heritage codes. Stripes, dots and Kate Spade Green, which we launched in partnership with

Pantone. This signature shade, which was featured an exclusive capsule across categories as well as updated recyclable and reusable packaging has been particularly successful with the brand's loyal fan base.

We're also continuing to engage with consumers through our social impact effort, which connects our customers to our brand beyond products. Taken together, our impactful marketing helped fuel the recruitment of approximately 400,000 new customers in North America. Additionally, we saw strong lapsed customer reactivation and an overall increase in spend per customer.

And finally, in keeping with our priority is becoming more global, we remain focused on meeting our target consumer where they shop around the world. To this end, we continue to roll out our new store concept, which began with Marina Bay Sands in Singapore in October. Since then, we have expanded the concept further to more than 15 doors across the globe, creating a compelling brand experience. And in Greater China, an area of opportunity for the brand, we launched Lunar New Year capsule collections, pop-ups and WeChat activations featuring our rabbit novelty offering, which drove strong engagement.

In addition, we collaborated with Starbucks China on a series of limited time-only merchandise to help build Kate Spade's brand awareness and excitement. The capsule had strong sell-throughs with more than half of the assortment selling out in just 2 days, signaling the brand's appeal to a broad base of Chinese consumers.

In summary, we continue to make progress in advancing the brand's, strategic growth agenda and see further opportunity ahead. Kate Spade is a unique lifestyle brand with global relevance, and we're making key investments to deepen consumer engagement through compelling products, marketing and experiences to drive sustainable growth and margin improvement over the long term.

Turning to Stuart Weitzman. In the third quarter, we delivered 10% revenue growth in constant currency, supported by double-digit growth in North America and a mid-single-digit increase in Greater China. Importantly, we achieved this top line performance while significantly expanding margins with higher full price selling driving gross margin gains.

Turning to the details of the quarter. We made further progress on our strategy to win with heat and improve brand awareness. First, we curated a highly relevant assortment of emotional product to spark desire. Our newer iconic families led our results with notable outperformance in pumps, booties and loafers. Soho was again a top collection, anchored by the on-trend Luxol which saw a strong performance with Millennial and Gen Z customers, while the Stewart family continued to grow and resonated across age groups. And our handbag collection, while still a small portion of the assortment, drove engagement with both new and existing clients at high AUR and accretive margins.

Second, we focused on creating compelling shopping experiences across the globe. As a result, we drove revenue growth in our global direct business, led by increases in North America, which included significant growth in digital. We also continue to strengthen our wholesale partnerships. Specifically, in North America, we saw an increase in sales at full price accounts while continuing to reduce off-price exposure as we focus on brand elevation. And internationally, we delivered continued growth as we increased our presence across key accounts.

Third, we fueled brand heat by leveraging new marketing tactics to increase buzz and organic awareness. This included an influencer back campaign with a compelling styling series to highlight our spring collection. In addition, we were pleased with the performance of our limited edition collection with KidSuper, a New York City-based streetwear brand and creative studio, which featured artistic plays on our icons that reach new customers across the globe at higher-than-average AUR. As a result of our focus on connecting with consumers in new ways, we drove an increase in the number of active customers in the quarter, fueled by engagement with our existing client base, including growth in reactivated customers.

Overall, we continue to advance our strategic initiatives to drive brand heat and awareness while maintaining financial and operational rigor to further support profitable growth. In closing, our third quarter results reinforce our progress in differentiating our brands and business. Although the environment remains uncertain, we operate in attractive durable categories from a position of strength with iconic brands amplified by a digitally enabled platform

that powers them to move at the speed of the consumer. We remain steadfast in our commitment to building enduring brands and relationships with consumers, and we're investing behind these priorities.

At the same time, we're being agile and disciplined financial operators. Controlling what we can control to successfully navigate the near term while advancing our long-term strategic growth agenda. Our runway is significant, and we have a relentless drive to deliver sustainable growth and value for all stakeholders.

With that, I'll turn it over to Scott, who will discuss our financial results, capital priorities and fiscal '23 outlook. Scott?

SCOTT A. ROE, CFO & COO, TAPESTRY, INC.: Thanks, Joanne, and good morning, everyone. As Joanne mentioned, we delivered significant top and bottom line outperformance.

In the quarter, we drove revenue growth of 9% on a constant currency basis, including 20% growth internationally. We expanded operating margin by approximately 280 basis points versus last year, led by gross margin gains and grew earnings per share by over 50%. Importantly, we also returned $270 million to shareholders, demonstrating our commitment to enhancing long-term value.

Turning to the details of the quarter, I'll begin with revenue, which will be shared on a constant currency basis. Sales rose 9%, well ahead of our expectations for an increase of 3% to 5% fueled by games both internationally and in North America. In Greater China, we returned to revenue growth in the quarter, driven by an improvement in traffic. Sales increased 20% with double-digit gains across stores, digital and wholesale. At the same time, we've started to see an uptick in domestic Chinese travel, including significant gains in our Hong Kong and Macau businesses as well as a pickup in Hainan. Importantly, although these initial reads have been encouraging, global Chinese tourist trends still remain well below pre-pandemic levels, representing an area of further opportunity.

In Japan, sales rose approximately 23%, while Other Asia grew 22%, driven by strength across Malaysia, Singapore, Australia, New Zealand and Thailand, with notable traction among local consumers. Sales to tourists also improved versus the prior year, although remained well below pre-pandemic levels. In Europe, sales increased 4%, fueled by gains with international tourists, notably from the Middle East. And in North America, sales rose 3%, driven by growth in January against last year's atypical comparisons related to COVID.

For the balance of the quarter and into April, trends in the region softened amid an increasingly challenging consumer backdrop. As such, we've incorporated a mid-single-digit decline in sales in North America into our fourth quarter outlook. By channel, our direct-to-consumer business grew 10%, led by a low-teens gain in stores as well as a mid-single-digit increase in digital. Importantly, we delivered higher operating margin in both channels relative to last year. And in wholesale, revenue was 7% below the prior year, reflecting growth in the international markets, fully offset by a decline in North America, which included a strategic reduction in off-price shipments.

Moving down the P&L. We delivered gross margin ahead of our projection and 290 basis points above prior year. This year-over-year expansion included approximately 360 basis points of favorable freight expense, partially offset by 120 basis points of FX headwinds. Therefore, excluding these impacts, gross margin was still ahead of the prior year, fueled by operational outperformance based on AUR increases, promotional discipline and a tailwind related to the increased penetration of higher-margin China business.

SG&A rose 5% compared to the prior year and included approximately $10 million of timing benefit with the fourth quarter. Throughout the quarter, we continued to prioritize high-return initiatives, including platform investments and brand building activities. Taken together, operating margin and operating income were ahead of our forecast and ahead of prior year. As a result, our third quarter EPS was approximately $0.20 ahead of our forecast, primarily due to $0.10 of operational outperformance as well as a favorable timing shift of $0.05 with the fourth quarter and roughly $0.05 associated with below-the-line benefits.

Overall, we delivered earnings growth of over 50% despite $0.10 of year-over-year FX headwinds.

Now turning to our balance sheet and cash flows. We ended the quarter with $652 million in cash and investments and total borrowings of $1.67 billion. There were no borrowings outstanding under our $1.25 billion revolver. Free

cash flow for the quarter was an inflow of $71 million including CapEx and implementation costs related to cloud computing of $57 million. Inventory levels for the quarter ended 2% ahead of prior year, favorable to our expectations on higher sales and tight inventory control. Given this performance, we're now well positioned to end the fiscal year with inventory approximately flat to last year as we continue to focus on higher inventory turn while delivering gross margin expansion.

Moving to our capital allocation priorities. We continue to plan for approximately $1 billion in shareholder returns in fiscal 2023, which consists of share repurchases of $700 million including $500 million repurchased fiscal year-to-date as planned and dividend payments totaling approximately $300 million. This is based on an annual dividend rate of $1.20 per share which represents a 20% increase over the prior year.

Our priorities remain unchanged. First, we're investing in the business to drive long-term profitable growth and second, we're returning capital to shareholders through dividends and share repurchases. In the future, we believe our platform is scalable and would evaluate M&A that is accretive to our organic TSR plan.

So moving to guidance. We're raising our fiscal year 2023 revenue and earnings outlook, which reflects our outperformance in the third quarter of $0.15, excluding the impact of timing. Let's touch on the details of this outlook, which replaces all previous guidance. For the fiscal year, we expect constant currency revenue growth of approximately 3%. On a reported basis, we anticipate sales to approach $6.7 billion, which is in the area of prior year and includes roughly 320 basis points of FX pressure. This implies constant currency revenue growth of approximately low single digits in the fourth quarter, excluding FX headwind of approximately 150 basis points.

Touching on sales details by region at constant currency. In North America, our guidance continues to contemplate a low single-digit decline for the year. As previously noted, this implies a mid-single-digit sales decline in the fourth quarter based on the increasingly challenging backdrop we're seeing. This also reflects our commitment to maintaining promotional discipline and higher margins as we manage our brands and our business for the long term. In Greater China, given the third quarter's outperformance, we anticipate a mid-single-digit gain for the fiscal year which includes an increase of approximately 50% in the fourth quarter.

In Japan, we expect to grow mid-teens, while other Asia is forecasted to grow 40%. And in Europe, we anticipate a high single-digit sales increase. In addition, our outlook includes a year-over-year operating margin decline in the area of 50 basis points, which assumes FX pressure of roughly 115 basis points. We expect the majority of this FX headwind to flow through the gross margin line. We anticipate gross margin to be approximately 100 basis points ahead of the prior year, largely reflecting the operational beat in the third quarter and the expectation for continued margin expansion in the fourth quarter.

For the full year, our gross margin forecast incorporates the benefit of moderating freight costs of 140 basis points as well as AUR growth, which is being partially offset by the previously anticipated rising input costs for materials as well as the negative impact of FX, as mentioned. On SG&A expenses, we anticipate deleverage for the year, reflecting growth-driving initiatives, including increased marketing expenses to fuel long-term customer value, investments in digital and the opening of our new fulfillment center in Las Vegas, partially offset by proactive actions we've taken to reduce our expense base.

Moving to below the line items. Net interest expense for the year is anticipated to be approximately $30 million, a significant decline versus fiscal '22, reflecting the benefit of our cross-currency swap agreements. The tax rate is expected to be approximately 19%, which is below our prior forecast given the lower actualization in the third quarter due primarily to geographic mix. Weighted average diluted share count is expected to be in the area of 242 million shares. This reflects approximately $700 million in share repurchases expected in the fiscal year as noted. Taken together, we project EPS of $3.85 to $3.90, representing a low double-digit growth rate compared with the prior year which includes a year-over-year currency headwind of approximately $0.40.

For the fourth quarter, this guidance implies earnings of $0.92 to $0.97, inclusive of the $0.05 timing impact with the third quarter. Finally, we now forecast CapEx and cloud computing costs to be in the area of $280 million. We expect approximately 30% of this spend to be related to openings and renovations with the majority of the balance

dedicated to our ongoing digital and IT initiatives, including investments related to our new fulfillment center in Las Vegas.

In closing, we delivered strong third quarter results with sales, margin and earnings growth all outpacing expectations, positioning us to raise our top and bottom line outlook for the fiscal year. In addition, we remain on track to return $1 billion to shareholders in fiscal '23, highlighting the power of our balance sheet and significant free cash flow generation. Importantly, our performance underscores our competitive advantages and reinforces our strategic agenda.

As we look forward, we remain focused on staying agile and discipline to deliver against our long-term priorities to drive sustainable, profitable growth and shareholder returns. I'd now like to open it up and take your questions.

Questions and Answers

OPERATOR: (Operator Instructions) We will take our first question from Bob Drbul of Guggenheim.

ROBERT SCOTT DRBUL, SENIOR MD, GUGGENHEIM SECURITIES, LLC, RESEARCH DIVISION: Can you discuss a little more in detail the demand backdrop that you're facing in North America and in China, how this impacts your view of the opportunity from here?

JOANNE C. CREVOISERAT: Well, we did deliver a solid quarter, which reinforces our confidence in our strategy and showcases the benefits of our globally diversified business and our direct-to-consumer business model. And I want to take a minute before I start to recognize our teams around the world who continue to drive our results.

We are pleased not only in our top line growth, but the significant gross margin expansion we delivered and we're deliberately managing our brands and our business for the long term. In North America, results in the third quarter were better than expected, although the trends did soften as the quarter progressed and that continued into April. The backdrop is increasingly challenging, and we are seeing a more cautious consumer. We've incorporated this trend into our guidance for Q4.

What you've seen in the third quarter is we're committed to being disciplined financial operators with a focus on driving healthy growth, both with a focus on margins and brand health. Conversely, our business in China is accelerating. As Scott mentioned, we drove double-digit growth in stores, online and in wholesale in the quarter. And importantly, at a constant currency basis, we're growing above our previous peak from FY '21. And I think another important fact is that we're building momentum with strong growth across the balance of Asia. And that business is now also about 15% of our total business.

And I just got back from being in China and Southeast Asia, and I am so impressed with our teams and how they've navigated the challenges in the environment. We've been in China with Coach, as you know, for 2 decades, and our teams are a differentiator. I saw this clearly during our travels. And it's a real competitive advantage for us. It's setting our brands apart, they're delivering innovation and connecting with our customers. And the confidence we have in our performance gives us long-term confidence.

Over the last 3 years, we've proven our ability to drive earnings growth in the face of a dynamic environment and headwinds in the market. The third quarter was no different. Our performance, I think, highlights our strength -- the strength of our globally diversified business, again, in our direct-to-consumer business model, and it showcases the strength of our brands around the world. We'll continue to build on this strength, and we see tremendous runway ahead across our portfolio.

OPERATOR: We'll take our next question from Ike Boruchow of Wells Fargo.

IRWIN BERNARD BORUCHOW, MD AND SENIOR SPECIALTY RETAIL ANALYST, WELLS FARGO SECURITIES, LLC, RESEARCH DIVISION: I guess maybe for Joanne and Scott, I wanted to ask, you've had several quarters under your belt now since your Analyst Day, you had the $8 billion target with $5 plus of earnings by '25. Can you maybe just comment on your thoughts on those targets at this point. Clearly, the revenue run rate

has been below, well you guys had hoped for, even though it is accelerating, which is great, but the margins seem like they have been better. So just trying to see confidence on both those top and bottom line expectations that you guys laid out multiyear.

JOANNE C. CREVOISERAT: I'll let Scott unpack the numbers for you, but we are gaining confidence in our strategy every quarter we deliver in over the last 3 years. But certainly, since our Investor Day, our teams continue to deliver on the priorities we laid out. And you can see by our results in the beaten rates we deliver today that those strategies are working, but I'll pass it to Scott, on targets?

SCOTT A. ROE: Yes, sure. Thanks, Joanne. Yes, we recently made comments around our confidence in the $5 plus EPS target that we laid out in our Investor Day, and we tell you a little bit why we had that confident in right? It's been a volatile and certain demand environment, and we're really focused on the things we can control, and there are certain things we can't.

But we're -- we said it repeatedly, we're not chasing the last dollar. We're being disciplined. And I think this year is a great testament to that. It certainly developed differently than we thought. But when we look at the way in which we're operating, the strong gross margin performance, coupled with our inventories being in great shape. It's evidence of strong discipline, the pricing power of the brand. And we continue to invest in growth longer term. And at the same time, using the great insight we have the 90% direct-to-consumer and that data. We're really rigorous on the returns on those investments and making sure that they're paying off and that they're driving future quality growth.

So you put these things together, and you're right, it's hard to see what the demand is going to look like, but we're gaining more and more confidence in our ability to deliver earnings just as we did this year, and we see that discipline being an even more important differentiator going forward.

Now a little bit about maybe the shape of that, just to help you, you're probably doing some modeling here, and many of you are, we would expect our path to $5 to be a little more weighted to '25 versus '24. And the reason for that is we've seen moderated North American performance, but we're a global diversified model, and we're seeing an acceleration in China. So you put those together, we see a little more back-weighted in '25.

OPERATOR: We'll move next to Lorraine Hutchinson of Bank of America.

LORRAINE CORRINE MAIKIS HUTCHINSON, MD IN EQUITY RESEARCH, BOFA SECURITIES, RESEARCH DIVISION: Has the promotional stance changed at all as trends fueled in North America? And what is your outlook for AUR and price increases over the next several quarters?

JOANNE C. CREVOISERAT: Well, Lorraine, the promotional environment exists. It always exists. I think we see an active promotional environment in the context of doing business in North America. But we have been very disciplined, in terms of how we think about our brands and our -- how we go to market. We continue to see pricing power across our portfolio. We delivered AUR gains and gross margin increases across the portfolio, and we expect that to continue. It really starts with great product, and our teams are innovating and delivering compelling products that consumers desire.

We're achieving and exceeding our revenue targets on higher gross margins again across the portfolio, which is evidence that being close to the consumer and delivering this product, it's working. We're going to remain agile. We do see further opportunity for AUR gains and gross margin growth. I think I'll probably kick it to Todd, who is Coach brand, which is further on the journey here to driving AUR gains and really understanding the customer and managing the business extremely well. So Todd, I'll let you add some color...

TODD KAHN, CEO & BRAND PRESIDENT OF COACH, TAPESTRY, INC.: Thank you, Joanne. And in the last 3 years, I've been waiting for that nonpromotional environment to come about. I haven't yet seen it.

What we have seen is in the last 3 years, we've increased our AUR by 30%. And I'm optimistic about the continued growth of our AUR at Coach for 4 main reasons. First, our innovation and storytelling, particularly when we talk

about handbags and SLGs. I think what you saw this last year since we've created expressive luxury is taking our purpose campaign and tying it to an actual product. And that is a differentiator from us and maybe our close-in competitors.

Second, something we've talked about quite a bit, emotion always trumps price. And when you look at the small bag phenomenon that we've experienced some of our highest fares, particularly in our value channel, command some of the smallest bags commanding the highest AUR. So we feel very good about that. Third, the white space that exists today between traditional European luxury, where Coach play is the largest we've ever experienced. So that gives us a lot of room to continue to show the consumer the value of our products.

And finally, something that both Joanne and Scott talk about quite a bit is our tight inventory control. Since we started our innovation and our transformation 3 years ago, we cut out about 50% -- almost 50% of our SKU count. That allows us to focus meaningfully on key family, which reduces the liability that we had historically had to carry. So I think those 4 things combined gives me a lot of confidence that we still have a way to go on AUR growth.

And as Scott said, we're not chasing top line. We are securing our margins, building a new customer base who are transacting at higher AURs.

OPERATOR: We'll take our next question from Matthew Boss of JPMorgan.

MATTHEW ROBERT BOSS, MD AND SENIOR ANALYST, JPMORGAN CHASE & CO, RESEARCH DIVISION: So Joanne, how would you assess if we take a step back, overall health of the handbags and accessories category globally today? And can you help walk through the functional drivers of the sustainable category growth that we've seen if you look back historically?

And then, Scott, maybe could you just speak to the profitability balance with investments that you're clearly striking, or any constraints that you see to executing against the multiyear double-digit earnings growth target that you've laid out?

JOANNE C. CREVOISERAT: Yes. Let me start with the handbag category. It is a resilient and durable category. And it has historically grown in that mid-to-high single-digit level for years. And it has proven, the category has proven going to be durable through downturns. And I think there are a couple of reasons that drive that.

One, the consumers have an emotional connection to this category, and we continue to get closer and closer to our consumers, particularly new and younger consumers coming into the market. To understand their needs and to appeal for both the emotional drivers of that category as well as the functional drivers of the category. There's a lot written about goods and services and where consumers are spending their money. But the handbag and leather goods category is a category that consumers use in all aspects of their lives. We saw demand even when people were locked in at home, and there was -- our stores were closed and people were going nowhere.

And then as the world reopened and people were going to social occasions and traveling more, going back to work, we saw a resurgence in demand and the resilience as people bring our products with them on those occasions. So I think the durability of the category speaks to both the emotional connection that consumers have as well as the functional needs that we support across all aspects of their life.

And the journey that we've been on in terms of brand building, it's really understanding the consumers' journey. We continue to leverage data to get deeper and deeper into those use occasions and their journeys and their needs emotionally and functionally and that's how we continue to deliver and deliver with pricing power.

As we look forward, we do a lot of research. There is still strong intent to spend in the category as we go forward. So we expect the trends to continue.

And then the second of your question....

SCOTT A. ROE: Yes, building on the second part. I think just going back to what Todd said earlier, it's -- our model right now and how we think about the trade-offs of profit and investment. We're not getting profit through SG&A cuts, right? We're getting it through quality growth.

And Todd's comment about leaning into engagement versus price, the discipline that goes around that, getting price increases driving those gross margins. That's why we're so focused on gross margins. that allows us to both continue to invest in the business and drive that emotional connection and at the same time, deliver profitability.

And just finally, linking back to what I said before, we're being really rigorous about making sure we're getting these investments. And some things work and we lean in, some things don't work, and we're quick to cut them off. And I think that's just the evidence of when we say disciplined operators. We're really looking at this with a lot of rigor right now.

OPERATOR: We'll take our next question from Brooke Roach of Goldman Sachs.

BROOKE SILER ROACH, RESEARCH ANALYST, GOLDMAN SACHS GROUP, INC., RESEARCH DIVISION: Joanne, I was wondering if you could elaborate a bit more on the changes that you saw in the North American consumer and their engagement with the brands in the back half of the quarter. What did you see in terms of traffic and conversion among various demographic cohorts? And then perhaps as a follow-up, how is customer acquisition and retention trending for Coach brand among the consumers that have been acquired since the acceleration strategy began?

JOANNE C. CREVOISERAT: So in terms of what we're seeing in North America, we're seeing the trends and the softness really more broad-based. So we're not seeing it targeted to any one specific consumer group. As we look across our business.

And as you may know, our brands and our customer average household income is around that $100,000 mark, and that's true across channels. And so what we saw in the quarter was just a generally more cautious consumer. And we are managing our business responsibly and to drive brand health. So continue to see pricing power within that context, but just a more cautious consumer overall. And that's what we've embedded in our guidance as we go forward so that we have realistic expectations about what the market is providing.

We're managing a global business. So we are seeing strength in other parts of our business. We have the agility to respond to those differing demand trends and continue to manage our business in a healthy way. So our outlook, and we raised our outlook shows that in our expectation for increased margin, continuing gross margins and continuing in Q4. So that's how we're thinking about the consumer and how we're managing our business. On consumer acquisition at Coach, yes, I'll pass it to Todd, maybe give you some color on that.

TODD KAHN: Yes. Thank you, Joanne. What we said this last quarter, we acquired over 800,000 new customers in North America alone. And if you look back at the last, almost a year, our customer acquisition is really doing quite well. And what we're seeing is our strategy of focusing in a younger Millennial and Gen Z consumer is working.

About half of the new customers are that younger cohort. Interestingly, they are transacting at higher AURs. So it is a self-fulfilling benefit to us. Additionally, what is important is we're retaining our existing customers. we're not firing our current customers. So we welcome everyone in the Coach family. But what I'd love to hear is, not only is it my brand for my mom, it's a brand for me now. And that's what we're hearing more and more and that's what's exciting. And that's what gives us confidence that our strategy is working.

OPERATOR: We'll take our next question from Oliver Chen of TD Cowen.

OLIVER CHEN, MD & SENIOR EQUITY RESEARCH ANALYST, TD COWEN, RESEARCH DIVISION: Coachtopia you have a lot of great underpinning there. I would love your thoughts on materials innovation and sustainability and how that may scale to Coach at large? And any details on cost of goods sold are longer and near-term implications for margin profile there?

And then as you speak to North America, you could speak to outlet relative to full price, any trends we should know about? And also your outlet channel continues to seem very vibrant (inaudible) as well as utilizing personalization and the customer data platform to drive differentiation and innovation. Just looked ahead with thinking about outlet and maintaining that and how yield balance the execution there relative to full price.

TODD KAHN: I was worried. I wasn't going to get my quota of questions for Coach, but clearly, we have achieved that now based on that. Joanne, I guess I'll take this and then you. Give some views on everything else. So Oliver, you're right about Coachtopia. It's been an overnight success, 2 years in the making. And we are very proud of what we've accomplished with Coachtopia.

And what we started off was this idea that both Coach and Tapestry do incredible work on sustainability, but we were always getting full credit for it. So we wanted to create a sub-brand that highlighted those efforts. We also recognized there was an opportunity to co-create with Gen Z and Millennials. And today, we have a community over -- a community of over 120 Coachtopians who are inspiring us and providing key input on the development of the product. We will be scaling Coachtopia.

I'd like to say this is not a vanity project, but we will be -- but it will become a large and profitable business. And you're exactly right in calling out that the concept of Coachtopia is to take learning that we've developed in product and material and usage of waste and applying those into coach. And over the longterm, that will have an absolute benefit in reducing our COGS. And so we're excited by that opportunity.

In outlet and in North America, I think it's key that we must and will continue to innovate product offerings and ideas through all of our channels. And we're seeing that. We're seeing great results in both brick-and-mortar outlet and outlet.com in North America as well as our full price business. And one of the things we've talked about in the past is our most valued customers in their lifetime value are those who shop in all 4 quadrants of our business. So we will continue to use data. We've experimented as Joanne said, both of us just came back from Asia.

One of the things we're doing so well in Asia is the outlet stores are some of the most beautiful, compelling stores in our fleet. We've put in Tabby product, full price, no discounting, and it's driving real sales there. So we're taking some of those learnings and applying them in the U.S. One of the opportunities is we've grown on both coach.com and coachoutlet.com, is that we see the consumer cross-shopping in a beneficial way.

So this opportunity, if a client of ours comes into a Coach outlet looking for Tabby, we want to satisfy that demand. So it's very exciting. I think there's a lot of opportunity for us to continue to grow both channels very profitably.

SCOTT A. ROE: Todd, yes, just to build on that, Oliver, too, just -- you asked a little bit about differentiation in channels, if I understood it right. We don't really see any material trend differences between retail or outlet across Tapestry, just for your information.

OLIVER CHEN: Just a quick follow-up on China. There's a lot of momentum there, but there's also at some retailers some conversion issues. So what do you see happening with the evolution of mainland consumption versus abroad? And there are some limitations with this and slight capacity. So would love your thoughts about what's embedded in guidance and perhaps risk factors that may or may not be out of your control?

JOANNE C. CREVOISERAT: Let me kick it off here, but we're winning in China, and we are seeing and able to capture momentum in the domestic market in China. And again, we talked about double-digit increase across all channels. We have a very strong brick-and-mortar presence in the market and 2 decades of experience in the market with understanding consumers. We've built a digital business and are on multiple platforms as we follow the consumer in the market.

So we feel very well positioned to meet and deliver -- meet that demand and deliver for customers in the market. To your point, we're seeing some shifts as they come out of the COVID restrictions. We're seeing more domestic travel. So we're capturing more business in Hong Kong, Macau, and in Hainan, which is a strong businesses for us. We have yet to see a resumption of international travel at the levels that it was pre-pandemic.

But again, we're driving significant growth in Southeast Asia, which is a market that the Chinese consumer used to travel to quite a bit. We're seeing and delivering significant growth today with a more domestic consumer. And we're well positioned in that market to capture the international inbound Chinese consumer as that unfolds as well as in Europe and in North America. So those trends have changed. We're not back to pre-pandemic levels of travel. We're capturing the demand we see in the mainland based on our deep experience there. And we are well positioned in the rest of the world as those international travel trends improve.

OPERATOR: And we'll take our final question from Mark Altschwager of Baird.

MARK R. ALTSCHWAGER, SENIOR RESEARCH ANALYST, ROBERT W. BAIRD & CO. INCORPORATED, RESEARCH DIVISION: A couple of quick ones for me. Just first, with respect to real estate, I was hoping you could touch on the outlook for the portfolio there. I think you had some net closures in the quarter, probably some seasonality. But just in the context of the ongoing strength you're seeing in digital channels, how should we be thinking about the runway there?

And then separately, with respect to gross margin, Scott, it looks like you're going to be approaching fiscal '21's high watermark this year. Maybe touch on some of the gross margin puts and takes beyond fiscal '23. It seems like freight is still an opportunity. You might be seeing some geographic mix benefits. Just wonder if there's any headwinds to be mindful of as we update our models?

JOANNE C. CREVOISERAT: Yes. I may kick it off with a question on our fleet. We were pleased actually to see the brick-and-mortar sales continue to grow. We drove low teens growth in brick-and-mortar. And I continue to say we have the best teams in the business and having customers and welcoming customers back to our stores gives us an opportunity to have our associates connect our customers more deeply with our brands.

And it's a terrific experience if you've been in our stores, hopefully, you know that. But we also have digital capabilities to meet the customer where they are. And that's proved to be a really strong investment, and we continue to improve the experience we're delivering both in brick-and-mortar but as well as online. And as we evaluate our fleet, we continue to prune and make sure that we have high profitability and productivity thresholds for our stores. And that's a constant evolution.

So you will see us make changes to our fleet, but we see opportunities to grow overall in stores. And as we laid out in our Investor Day, we see the opportunity to grow our store fleet. I think we said 100 stores growth over that time period, 50 to 100 stores of growth over that time period. And most of that store growth we see happening in Asia. So in the other markets, you'll see us open some and maybe close on relocate, remodel.

But maybe I'll pass it to Scott, he can give you the actual numbers, but that's how we think about, strategically think about the fleets and managing it.

SCOTT A. ROE: Yes, you had it, Joanne,around 100, 80, I think Christina is telling me 70. So -- but the important thing is we're managing our lease terms effectively. We can turn the entire fleet. We have about a 4-year average term. And underneath that, we're always finding certain areas that are trending down, and we're moving out of those and we're finding new areas that make sense given our insight into the consumer and where they're at and where they want to shop. So there's what I call the normal hygiene that's going on underneath that. But no huge changes in the fleet size is just the growth, which is mostly outside of the U.S.

As it relates to gross margin, just a quick comment. We're obviously not going to give any guidance or specifics. But if you think about it, there is puts and takes that are always happening. We see leather prices moderating. We continue to see hardware and some of the other componentry having upward pressure, labor is a continued upward pressure. But to me, the most important thing is what Todd said earlier, it's the focus on engagement with the customer, the insights that we have and increases our bag in average to make good decisions. We're investing behind the brands. And ultimately, that means pricing power.

So why do I have confidence in our gross margin, it's pricing power, the insights that we have. The shape of the business will help us a little bit as we go forward to the recovery of China and our Asia business is generally higher margin too. So from a mix standpoint, that will benefit us over time.

OPERATOR: That concludes our question-and-answer session. I will now turn it over to Joanne for some concluding remarks.

JOANNE C. CREVOISERAT: Thank you for joining us today and for your interest in our story. Today, we reported a strong third quarter and raised our outlook for the full year. This is a testament to our incredible global teams who continue to drive our results.

Our performance also reinforces the power of our brands and our globally diversified direct-to-consumer business model. These competitive advantages are clearly differentiated results. We're confident in our strategy and our runway is significant. We remain focused on driving sustainable growth and shareholder returns into the future. Thanks again, and have a great day.

OPERATOR: This concludes Tapestry's Earnings Conference Call. We thank you for your participation.

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